No. 86-1612

IN THE

Supreme Court of the United States

October Term, 1986

CONSOLIDATED RAIL CORPORATION,

Petitioner,

v.

ERIE LACKAWANNA INC.,
JOHN HENNING, and VICTOR LaSCALA,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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COUNTER-STATEMENT OF THE QUESTION PRESENTED

Whether the district court properly barred claims first asserted after the termination of a former railroad's bankruptcy proceeding, in respect of which Congress in the Rail Act had granted the court broad discretion to liquidate the assets remaining to the bankrupt railroad after the mandatory conveyance of its rail assets to Conrail, where the district court effected the bankrupt's liquidation and the distribution of its remaining assets to allowed creditors, at 52¢ per dollar of their allowed claims, through the vehicle of a liquidating corporation?

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Respondent Erie Lackawanna Inc. ("Erie")[1] respectfully submits this brief in opposition to the petition for

1. Pursuant to Rule 28.1 of the Court, Erie provides the following listing: (1) parent companies: none; (2) subsidiaries (other than wholly-owned subsidiaries): Niagara Junction Railway Co. (minority interest).

writ of certiorari ("Pet.") of Consolidated Rail Corporation ("Conrail").

COUNTER-STATEMENT OF THE CASE

This case turns on the application of two virtually obsolete statutes — the Regional Rail Reorganization Act of 1973 (the "Rail Act") and Section 77 of the now repealed Bankruptcy Act of 1898[2] — to the unique facts of one former railroad's bankruptcy proceeding under those statutes. The judgment which petitioner asks the Court to revisit was reached unanimously by all four judges who considered the merits of the question.[3] Not a single judge of the Sixth Circuit requested a vote on Conrail's petition for rehearing en banc (A–39).

Petitioner's Statement of the Case suggests that the court of appeals established a major precedent for pending and future reorganization proceedings. Yet a balanced summary of the proceedings shows that the opinion below can have no such impact. Notwithstanding petitioner's extravagant assertion that the court of appeals fashioned a means by which corporations can misuse generally applicable federal bankruptcy statutes, it is clear that the decision below was based on provisions of the Rail Act and Section 77 which do not apply to reorganizations in general and which have no further applicability even to railroad reorganizations. The only interest at stake on this petition for writ of certiorari is Conrail's claim to

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2. The Bankruptcy Act of 1898 was superseded on October 1, 1979 by the Bankruptcy Reform Act of 1978.

3. The order of the district court affirmed below had been entered by the Hon. Robert B. Krupansky, United States Circuit Judge for the Sixth Circuit, sitting by designation on the district court, where he had presided over the bankruptcy proceeding as a district judge beginning in 1972. Judge Krupansky's order was affirmed by a unanimous panel of the court of appeals.

indemnity from the former creditors of the defunct Erie Lackawanna Railway Company and their assignees — a claim that was correctly resolved against petitioner after full and fair hearings in the two lower courts.

A. Background

In 1972, the Erie Lackawanna Railway Company (hereinafter referred to as "the Debtor" to distinguish it from respondent Erie) filed for relief under Section 77 of the Bankruptcy Act of 1898, a special railroad reorganization statute (formerly codified at 11 U.S.C. § 205) which, for reasons of national transportation policy, did not provide for liquidation of a debtor even if the debtor lacked sufficient earning power to continue its rail business as a reorganized carrier (A–6, A–9). Most of the railroads in the northeastern United States were in similar straits, and Congress recognized that the mechanism of Section 77 could not cope with so massive a problem. It therefore enacted the Regional Rail Reorganization Act of 1973 ("the Rail Act"), 45 U.S.C. §§ 701–797. The Rail Act created Conrail, required the bankrupt northeastern railroads to transfer their rail businesses to Conrail, and thereby effected a reorganization of those businesses entirely outside the framework of the Bankruptcy Act (A–2, A–9).

The mandatory conveyance of rail assets to Conrail which occurred on March 31, 1976 left the bankrupt railroad companies with the right to compensation from the United States for the property taken by Conrail, with miscellaneous assets, and with massive debts. Their estates were still in the custody of various district courts because of the pending Section 77 proceedings, and Section 601(b)(4) of the Rail Act (45 U.S.C. § 791(b)(4)) directed each court

> to reorganize or liquidate such railroad in reorganization pursuant to Section 77 on such terms as the court deems just and reasonable, or pursuant to any other provisions of the

> Bankruptcy Act, if the court finds that such action would be in the best interests of such estate.

The Rail Act thus explicitly empowered the district court to order liquidation of a debtor under Section 77, even though that Section did not contemplate liquidation and provided no rules or procedures for liquidation. In view of this statutory void, Congress vested broad discretion in the district court to liquidate the remaining assets of the former railroads "on such terms as the court deems just and reasonable."

In the instant case, the Debtor's liabilities far exceeded its assets, even after it had received more than $300 million (including interest) in compensation from the United States for the assets conveyed to Conrail, and the Debtor had retained no income–producing assets around which to mold an operating company.[4] Consequently, in 1982 the district court found the Debtor's stock to be worthless (A–48, A–51). It ordered that the sole stockholder receive nothing, that the cash assets be used to satisfy claims of secured and other priority creditors, and that the then remaining non–cash assets be liquidated over a six–year period for distribution of the proceeds (together with any remaining cash) to general creditors. Such distribution was effected by the issuance of the stock of what Judge Krupansky called the "liquidating corporation," *i.e.*, respondent Erie, provided for in what was denominated as the Debtor's plan of reorganization (the "Plan") (A–40). All proceeds realized from the liquidation and other cash earned from investment thereof were ordered to be placed in a Master

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4. Petitioner incorrectly states that "[t]he Reorganized Company has exploited the value of the [Debtor's] net operating loss carry forwards. . . ." (Pet. at 13). On the contrary, the Debtor's losses referred to by petitioner were insufficient to offset the taxable interest income received by the Debtor prior to consummation of the plan for the assets conveyed to Conrail (A–90 to A–91).

Trust to assure payment of the priority claims (A–62 to A–63).[5]

Upon consummation of the Plan on November 30, 1982, the district court entered a Final Decree barring after-asserted claims. The decree permanently enjoined all persons from instituting any lawsuit against the liquidating corporation "based upon any right, claim or interest of any kind or nature whatsoever . . . against the Debtor . . . ." (A–129).

Contrary to petitioner's insinuations that Erie is an ongoing, profitable business (*e.g.*, Pet. at 11), Erie's sole authorized activity is the disposition of the remaining assets for the benefit of general creditors and their assignees, the investment of the Master Trust moneys pending distribution, and the settlement of tax liabilities and other claims asserted before consummation of the Plan but not then resolved (A–48 to A–49). In other words, petitioner seeks to enforce indemnity claims first asserted after the bar date, November 30, 1982, against assets already allocated by the court to carry out the satisfaction of allowed creditor claims at a loss.[6]

Under the broad discretion conferred upon the district court by the Rail Act, Judge Krupansky after March 1976 might have converted the Section 77 proceeding into a statutory liquidation under the Bankruptcy Act. But the

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5. Under the terms of the Master Trust, the investment of all Master Trust moneys is restricted to risk-free or low-risk securities, and, except for the payment of priority claims and taxes and for working capital required to effect the liquidation, no assets may be withdrawn prior to the payment of all priority claims without approval of the district court (A–62 to A–63; A–224 to A–228; A–232 to A–233).

6. The circumstances of the Debtor in this case, therefore, differed substantially from those (for example) of the Reading Company and the Central Railroad of New Jersey — the ex-railroads involved in *Schweitzer v. Consolidated Rail Corp.*, 758 F.2d 936 (3d Cir.), *cert. denied*, 106 S. Ct. 183 (1985). Neither of the reorganization plans of those railroads was a liquidating plan.

mechanism he chose instead — a liquidating corporation combined with a Master Trust — had compelling administrative advantages. Statutory liquidation would have subjected to the district court's supervision the sale of hundreds of pieces of remaining property, primarily unimproved real estate. This cumbersome procedure would have increased the administrative cost of liquidation and burdened the district court for no good reason, since the court's role as referee among the conflicting interests was no longer needed: the stockholder's interest had been completely extinguished, priority claims had all been provided for with cash pursuant to the liquidating plan, and the remaining creditors had agreed to be treated as a single class for pro rata distribution of the deficient residue.[7] Another disadvantage of straight bankruptcy was the burden upon trade creditors who had no marketable securities evidencing their claims and would have to wait many years for pro rata distribution.

Both these problems were solved by the court's use of a liquidating corporation. This vehicle eliminated the need for court orders to authorize sales of remaining assets and permitted issuance of marketable securities — the new Erie capital stock — to unsecured creditors. The new capital stock was issued at the rate of one share per $100 of allowed claim. Its book value, however, was only $52 per share, and its market value upon issuance was substantially below book value (A–3, A–67, A–234).

The Plan approved by the district court *mandated* the sale of *all* the Debtor's assets and *mandated* the transfer of the proceeds of sale to the Master Trust for the benefit of allowed

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7. The liquidating plan of reorganization made possible the approval under Section 77(e) (A–199 to A–200) of a large number of compromises of position among the various types of creditors as to priorities and amounts of valid claim without the necessity of either obtaining 100% approval by such creditors or litigating the issues to the bitter end that "straight liquidation" would have entailed.

priority creditors. As required by former Bankruptcy Rule 8–404(b), the Plan provided a five–year waiting period during which creditors were permitted to exchange debt certificates and executed satisfactions of claims for the consideration provided in the Plan. Approximately one year thereafter, dissolution of the liquidating corporation is required pursuant to both the Plan and Erie's charter, which state that Erie is "to be completely liquidated." The only way that dissolution can be avoided is by a charter amendment approved, after all claims have been paid or provided for, by a vote of not less than 75% of all stock outstanding, coupled with an appraisal right and payout to any dissenting shareholder who demands it (A–68 to A–69).[8]

B. The Proceedings Below

Two years after the Final Decree, several former employees of the Debtor brought suit against petitioner Conrail and in some cases against Conrail and the liquidating corporation, respondent Erie, for alleged personal injuries. Petitioner Conrail brought suit against Erie claiming indemnity for Conrail's liability on such personal injury claims. For the purpose of this case, it was assumed that these injuries did not become manifest until after consummation of the Plan, but were caused (at least in part) by on–the–job exposure to asbestos or other pathogens before 1976, while the Debtor was an operating railroad.[9]

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8. Early in 1984, the Erie Board of Directors resolved to seek a vote extending Erie's life after final determination of Erie's tax liabilities and assuming no intervening material adverse events. This resolution was rescinded in May 1986 for reasons unrelated to this case.

9. One of the indemnity claims does not involve personal injury but Conrail's liability to the State of New York for a petroleum leak on property conveyed to Conrail by the Debtor. Moreover, in at least one of the personal injury cases involving a third–party claim by Conrail against Erie, Conrail was sued prior to the consummation date but did not commence its third–party claim until after that date.

In response to these claims, the liquidating corporation applied to Judge Krupansky for an order declaring that such suits were barred by the injunctive provisions of the Final Decree and for an injunction requiring their dismissal. Judge Krupansky granted the relief requested, holding, *inter alia*, that the Debtor–tortfeasor no longer exists and that the liquidating corporation is not the Debtor's successor — indeed, is not an ongoing business at all, but merely a vehicle for liquidation (A–10, A–32).[10]

Conrail and two personal injury plaintiffs, respondents Henning and LaScala, appealed to the Sixth Circuit. On that appeal, a unanimous panel of the Sixth Circuit affirmed Judge Krupansky's order. It held that the liquidating nature of the Debtor's bankruptcy proceeding was dispositive and that the Rail Act gave the district court sufficient flexibility to bar after–asserted claims in a Rail Act–Section 77 reorganization–liquidation to the same extent as such claims would be barred in statutory liquidation (A–7 and n. 4). Since not even non–discharged claims can be enforced in "straight bankruptcy" so as to diminish the pro rata share in the estate of creditors whose claims — like those of the creditors who became the shareholders in the liquidating corporation — were filed before the bar date and allowed by the court, the court of appeals did not reach the question of discharge *vel non* presented in *Schweitzer v. Consolidated Rail Corp.*, 758 F.2d 936 (3d Cir.), *cert. denied*, 106 S.Ct. 183 (1985) (A–2 n. 1). Conrail's petition for rehearing en banc was denied.

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10. Judge Krupansky also went on to analyze at length — and reject — the petitioner's argument below that its claims were not discharged for the reasons stated by the Third Circuit in *Schweitzer*. Judge Krupansky declined to follow *Schweitzer*.

REASONS FOR DENYING THE PETITION

In order to conjure up an issue worthy of certiorari, petitioner first distorts the record of the Debtor's bankruptcy proceeding and the opinion of the court of appeals and then asserts that the Sixth Circuit has devised a new form of reorganization that is both unauthorized by federal bankruptcy statutes and in conflict with decisions in other circuits. Nothing could be further from the truth. The judge who presided for ten years over the Debtor's Rail Act–Section 77 proceeding understood the liquidating nature of that proceeding. Based on that understanding, he explicitly found that respondent Erie is not an ongoing business and is not the Debtor's successor. In holding that petitioner cannot pursue its claims against respondent Erie as if it were the Debtor's successor, the court of appeals did not "concoct" anything "retroactively" (Pet. at 7). Rather, it correctly applied the Rail Act and Section 77 to the facts found by the district court and fully supported by the record.

The Rail Act was enacted to supplement Section 77 of the Bankruptcy Act and to establish a special form of reorganization of the railroad businesses of only a designated handful of bankrupt railroads at a particular time (1973) and place (the northeastern United States). Section 77 has no prospective applicability, and the Rail Act's narrow objective has now been accomplished. This case is doubtless one of the last that will arise under any provision of those acts, and the opinion of the court of appeals is of no significance for bankruptcy proceedings in general.

Moreover, the decision below does not conflict with the decisions of the Eighth and Ninth Circuits cited by petitioner; nor can it so conflict in view of the fact that neither of those cases was governed by the statutes whose construction controls here. Nor is the "absolute priority rule" in any way implicated in the dispute between Conrail and Erie. All that is at stake on the petition is whether it was "just and reasonable"

for Conrail to be barred from diluting the already deficient distribution to allowed creditors of the defunct Erie Lackawanna Railway Company by enforcing new indemnity claims against a fund previously allocated by the district court. The courts below have resolved this dispute between Conrail and Erie; since nothing more is at stake, the petition should be denied.

A. The Sixth Circuit Correctly Interpreted the Rail Act

After ten years of bankruptcy proceedings, the district court determined that allowed claims against the defunct Erie railroad far exceeded its assets; that the shareholder's equity was worthless and would be wiped out; that all business operations of the Debtor had permanently ceased; and that the Debtor's property should be liquidated for the satisfaction of priority claims and distribution of the residue to allowed general creditors at 52¢ per dollar of allowed claim.

This case arises solely because of the administrative mechanism chosen by the district court to carry out these determinations. Petitioner acknowledged below and acknowledges here (Pet. at 10) that the court had the power under the Rail Act to accomplish the result it deemed "just and reasonable" by explicitly converting the Section 77 proceeding into a statutory liquidation.[11] If it had done so, there is no question that petitioner's claims would be barred (*see* opinion at A–5, A–7). The rule in statutory liquidation is that only claims filed prior to the bar date can participate in pro rata distribution of the bankrupt's estate; claims "not filed within the [prescribed] time" may be paid *only* out of the surplus —

11. Unlike Chapter X, relied on by petitioner, Section 77 itself did not permit such conversion; the court's power to convert is derived solely from the broad discretion granted by Section 601(b)(4) of the Rail Act, as petitioner acknowledges.

if any — remaining after "all claims which have been duly allowed have been paid in full." Bankruptcy Act § 57n, former 11 U.S.C. § 93(n). The bar date in statutory liquidation is absolute, and no justification or excuse permits a late claim to dilute the discounted pro rata share of allowed creditors. *See, e.g., In re Pigott*, 684 F.2d 239, 245 (3d Cir. 1982); *Tarbell v. Crex Carpet Co.*, 90 F.2d 683 (8th Cir. 1937); *In re Sullivan*, 36 Bankr. 771 (Bankr. E.D.N.Y. 1984); *In re Weis Securities, Inc.*, 411 F. Supp. 194 (S.D.N.Y. 1975), *aff'd per curiam*, 538 F.2d 317 (2d Cir. 1976).[12]

Here, there was no surplus; the Debtor's estate was insufficient to satisfy the timely filed creditor claims in their allowed amount. The absence of any surplus over such creditors' claims was so clear in the Debtor's case that the Debtor's sole shareholder never sought at any time during the entire proceeding to participate in the estate. General creditors received value of only 52¢ per dollar of the allowed amount of their claims, and thus there was nothing left for post–consummation claims.[13]

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12. Conrail is thus mistaken when, citing provisions of Section 77, it says that the former employees here involved would have had priority in a "true liquidation" over the claims of the unsecured creditors (Pet. at 13). If the proceeding had been converted to a statutory liquidation, Section 57n of the Bankruptcy Act would have governed. If Judge Krupansky had converted Erie's proceedings to a straight liquidation following the conveyance of the rail business of Erie in 1976, the bar dates provided in Section 57n would have expired far earlier than the bar date of November 30, 1982 established in the court's decree.

13. Much of the increase in book value of the stock of Erie since consummation of the Plan in 1982, to which Conrail refers (Pet. at 13), is due to the interest income earned since 1982 on the moneys in the Master Trust ultimately distributable to the Debtor's general creditors (now the Erie stockholders). The general creditors have not yet received any cash on account of the stock issued under the Plan.

Petitioner's argument amounts to a claim that Judge Krupansky erred in barring its claims because the mechanism he had chosen for liquidation was a "liquidating corporation" created by a plan adopted under Section 77 rather than a statutory trustee. To bolster this argument, petitioner inaccurately states that the Rail Act limited the district court to only two choices: "to reorganize under Section 77 or to liquidate pursuant to some other section of the Bankruptcy Act" (Pet. at 10). However, the Rail Act did not put the district court in the strait jacket suggested by petitioners. Rather, it explicitly authorized the district court, as one of its options, to liquidate under Section 77. Recognizing that Section 77 did not itself provide a mechanism for liquidating a railroad, it then granted the court the discretion to "liquidate such railroad in reorganization pursuant to Section 77 on such terms as the court deems just and reasonable . . . ."

To further bolster its argument, petitioner asserts that the courts below allowed the Debtor to "enjoy the benefits" of reorganization, "continue in operation in perpetuity," reap "equity–type rewards [without] equity–type risks," operate "as a profitable corporation," and "sail unencumbered into the twenty–first century." (Pet. at 7, 11, 13). On the contrary, the courts below premised their decisions on the fact that the Debtor's equity and business had ceased to exist altogether, and that respondent is nothing more than a vehicle for liquidating the business property and holding the proceeds in banks or low–risk debt instruments until they are distributed to the allowed creditors and their assignees, whereupon Erie will be "completely liquidated" as required by the Plan.[14]

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14. Petitioner seeks to avoid the uniqueness of these facts by misleadingly suggesting that the Special Court established under the Rail Act has recently found "that the Reorganized Company was in the same position as several other former railroads that had conveyed rail assets to Conrail and reorganized as non–railroads." (Pet. at 11–12, n. 3). However, the Special

While petitioner relies heavily on the provision of the Plan which allows the liquidating corporation to continue in existence (after all prior claims have been provided for) upon a vote of at least 75% of the shares outstanding, the court of appeals correctly noted (A–7 to A–8) that the unlikely event of such a supermajority vote does not change the economic reality that the Debtor's business has completely ceased to exist. After completion of disposition of all the property, the Debtor's assets will have been reduced entirely to cash, which 75% of its former general creditors might theoretically pool and reinvest in a new and entirely unrelated common enterprise within the corporate shell of respondent.[15] Any future decision of Erie's creditor–stockholders to continue to pool their distributive shares would not alter the fact that, under the circumstances of this case, the distribution to those creditors constituted a liquidation of the Debtor which insulated the distributees and their assignees from post–liquidation claims based on pre–1976 operations of the Debtor. As the court of appeals correctly stated, "[i]f a straight liquidation was ordered, nothing would prohibit the unsecured creditors from embarking on a new business enterprise with the funds they received, without the worry of a lawsuit." (A–7).

The form of liquidation chosen by the district court was not crafted to enable Erie to "sail into the twenty–first century" while "operating a profitable corporation." Its sole

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Court opinion cited by petitioners had nothing to do with Section 601(b)(4) of the Rail Act. Rather, the Special Court merely held that Section 709(b) of the Rail Act neither provided an explicit basis for recovery against Conrail by former employees of the bankrupt railroads nor insulated Conrail from liability under tort law theories of successor liability. In reaching that conclusion, the Special Court merely noted that, like the other railroads before the court, the Debtor's Section 77 proceeding had been terminated.

15. That such a vote would be equivalent to a voluntary new investment of cash by each ex–creditor is made clear by the absolute right of any shareholder dissenting from the vote to withdraw his share of the cash (A–68 to A–69).

purpose was the efficient administration of the estate and the maximization of net proceeds available for distribution to creditors. Statutory liquidation would have required wasteful and cumbersome court proceedings to approve the sale of the Debtor's miscellaneous pieces of property, and would have deprived those trade creditors who needed ready cash of an efficient market in which to sell assignments of their interest in the liquidation.[16]

Petitioner's contention (Pet. at 13–14) that on the basis of the decision below "any corporation in bankruptcy" will be encouraged to structure its reorganization to include a "liquidation option" and thus cut–off post–consummation claims is ridiculous. The Rail Act does not apply to "any corporation in bankruptcy" and does not even apply to future railroad reorganizations. Moreover, the decision of the court of appeals below was not based on any "liquidation option;" on the contrary, it was based on the mandated cessation of the Debtor's business and the requirements of the Plan that *all* assets be liquidated and reduced to cash and that all proceeds of the liquidation be placed in trust subject to severe restrictions. What corporation able to effect a true reorganization of any part of its business would ever prefer such a suicidal procedure? Given that in the great majority of corporate reorganizations there are assets sufficient to permit participation by the stockholders in the reorganized business, the possible use of this case, where no surplus for stockholders

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16. Petitioner argued below that its claims were enforceable against Erie because the liquidating corporation was established by charter amendment rather than dissolution and reincorporation. This argument that the district court was required to follow a particular form in order to achieve the result it "deemed just and reasonable" is inconsistent with the Rail Act and was properly rejected below. Reincorporation would have required the burdensome and expensive conveyancing and recording in the name of the new corporation of hundreds of parcels of real property located in several states, even though the liquidating corporation was to sell the real estate as soon as practicable after consummation.

existed, as a "persuasive precedent" in barring post-consummation claims in other corporate bankruptcy proceedings, even by analogy, is highly remote indeed.

Compelling considerations of administrative efficiency led the district court to conclude that a hybrid form of liquidation was "in the best interests of such estate." The court of appeals correctly held that Section 601(b)(4) of the Rail Act gave the district court sufficient flexibility to do so (A–7 and n. 4). As the court of appeals held, the district court's orders making provision for priority creditors to be paid in cash and directing the distribution to the general creditors of Erie's stock constituted the liquidation of the Debtor under a plan with terms which were "just and reasonable." For the foregoing reasons, the writ of certiorari should be denied.

B. The Decision Below Does Not Conflict with Decisions of the Eighth and Ninth Circuits

Petitioner asserts that the opinion of the court of appeals is in direct conflict with the decisions of the Eighth and Ninth Circuits in *Bankers Life & Casualty Co. v. Kirtley*, 338 F.2d 1006 (8th Cir. 1964) and *Kelce v. U.S. Financial Inc.*, 648 F.2d 515 (9th Cir. 1980), *cert denied*, 451 U.S. 970 (1981). However, the facts of those cases do not remotely resemble the facts below, and the holdings of the Eighth and Ninth Circuits do not in any way address the issue before the court of appeals below. The opinion of the court of appeals, a correct application of the Rail Act to unique facts, simply does not conflict with the decision of any other federal court.

In *Bankers Life & Casualty Co. v. Kirtley*, a Chapter X proceeding, the district court had ordered equitable subordination of the interest of two controlling stockholders to that of the debtor's public stockholders. The controlling stockholders appealed, claiming that the district court lacked the power of equitable subordination because the reorganization plan called not for rehabilitation but for

liquidation of the debtor's assets. Arguing that liquidation is not concerned with equities among stockholders after the rights of creditors are satisfied, the controlling stockholders claimed it was reversible error for the district court to exercise equitable powers expressly granted by Chapter X in a Chapter X proceeding which contemplated liquidation. The Eighth Circuit rejected this argument and affirmed. It noted that Chapter X rules specifically permitted the sale of all of the debtor's assets (*i.e.*, a liquidation) and modification of the rights of stockholders. The court held that it was not error for the district court to apply these specific Chapter X rules in a Chapter X proceeding.[17]

In *Kelce v. U.S. Financial Inc.*, a defrauded shareholder sought reversal of an order subordinating his fraud claim to those of general creditors. The Ninth Circuit affirmed, holding that it would violate the absolute priority rule to allow a stockholder to share in the debtor's estate on equal footing with unsatisfied creditors. Citing *Bankers Life*, the Ninth Circuit in dictum in a footnote rejected the appellant's attempt to distinguish the rationale given by commentators for subordinating a shareholder's fraud claim to claims of creditors. Appellant had urged that the commentators' arguments did not apply to a Chapter X reorganization in which liquidation was the ultimate goal, and the Ninth Circuit disagreed.

Even the most cursory analysis makes clear that the opinion of the court of appeals below does not conflict in any way, let alone directly, with these decisions. Both *Bankers Life* and *Kelce* involved the formulation of reorganization plans and questions with regard to the application of Chapter

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17. In holding that it was not error for the district court to apply Chapter X rules in a Chapter X proceeding, the court in *Bankers Life* did not address whether it would have been improper for the district court to fashion a plan utilizing other bankruptcy rules.

X rules to claims asserted during the course of Chapter X reorganization proceedings. Neither case involved the Rail Act's broad grant of discretion to the district court to liquidate the debtor "pursuant to Section 77 on such terms as the court deems just and reasonable." More importantly, those cases are concerned only with rules on issues concerning priority of claims that apply in formulating a plan; neither case addressed the issue here involved, *i.e.*, whether claims filed after consummation of a liquidating plan are barred as against creditors by reason of the liquidating nature of the plan.

Petitioner also asserts that the court of appeals below completely misread the effect of the liquidation of a corporate debtor and ignored "fundamental bankruptcy law" in barring petitioner's claims (Pet. at 12). This argument is astonishing given petitioner's concession below that claims filed after the bar date in a straight bankruptcy liquidation could not be enforced against the interest of allowed creditors. The fact cited by petitioner that "liquidation would not have discharged [the claimants'] claims" (Pet. at 12) simply is irrelevant and was properly not addressed by the court of appeals. Not even non–discharged late claims can be enforced in straight bankruptcy so as to diminish the pro rata share in the estate of creditors whose claims were filed before the bar date and allowed by the court. A non–discharged claim which is filed after the bar date can be satisfied only out of the surplus, if any, available for the stockholders. Here, there was no surplus.

In citing to *Kelce*, petitioner underscores the importance to bankruptcy proceedings of fulfilling just expectations (Pet. at 10). Here, the just expectations of participants in the Debtor's bankruptcy proceeding would be thwarted if petitioner's position prevailed. Contrary to the assertions of petitioner, the Debtor's creditors did not bargain for equity–type rewards in exchange for equity–type risks (Pet. at 11). As the court of appeals correctly recognized (A–6 to A–7), it is factually incorrect to speak of the creditors as accepting the

risk of Erie's "business." Erie has no business; the Plan extinguished all equity interest in the Debtor and provided that the *only* activities of Erie would be those required for its liquidation. In such circumstances, permitting petitioners now to enforce their claims would improperly dilute the allowed claims of the Debtor's creditors and would frustrate the creditors' legitimate expectations that the compromises made in the liquidation plan would be accorded finality.

C. The "Absolute Priority Rule" Has Nothing to Do with This Case

Petitioner argues that the decision of the court of appeals "conflicts with both the congressionally mandated claim priority scheme and the absolute priority rule pronounced by this Court." (Pet. at 14). For two reasons this argument does not warrant review by this Court.

First, while personal injury claims of a railroad debtor's employees were entitled to priority under Section 77, petitioner is not a former employee of the Debtor and is not asserting a personal injury claim. Rather, petitioner Conrail is a billion–dollar public company asserting an indemnification claim against the liquidating corporation while at the same time denying its liability to the Debtor's former employees. Most of the individual former employees of the Debtor whose claims were the subject of the proceedings below did not appeal the district court's decision barring their claims as against Erie, and the two individuals who pursued their appeals in the Sixth Circuit, respondents Henning and LaScala, have not petitioned for certiorari.

Second, the decision below clearly does not violate either the Section 77 priority granted employee personal injury claims or the absolute priority rule. As petitioner conceded below, claims filed after the bar date in a straight bankruptcy liquidation could not be enforced against the interests of allowed creditors. *See* Section 57n of the Bankruptcy Act of 1898. Even as to priority claims, there comes a cut–off time

where the assets of a liquidating, insolvent corporate debtor are allocated among qualifying creditors then present, whereupon the Debtor becomes a "judgment proof" empty shell.

Nothing in *Northern Pacific R.R. v. Boyd*, 228 U.S. 482 (1913) and its progeny is to the contrary. While *Boyd* recognized the right of a creditor who did not participate in a reorganization to subject the interests of a Debtor's old stockholders to his claim, *Boyd* specifically recognized that "[i]f [the stockholders'] interest is valueless, [the creditor] gets nothing." 228 U.S. at 508. Here, the district court found in 1982 that the Debtor's stock was worthless. The court, therefore, properly barred petitioner's post–consummation claims.

CONCLUSION

For the foregoing reasons, the petition for writ of certiorari should be denied.

Dated: May 6, 1987

Respectfully submitted,

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